Gurukripa's Guideline Answers to May 2014 Exam Questions
CA Final DIRECT TAXES

Question No.1 is compulsory **(4 × 5 = 20 Marks).**

Answer **any five** questions from the **remaining six** questions.

All questions relate to the Assessment Year 2014–15, unless stated otherwise in the question.

Note: All Page Numbers and Question Numbers References are given from Padhuka's Direct Taxes – A Ready Referencer – CA Final.

Question 1(a): Sec. 80–IB, Surcharge, Filing of Return on Various dates (10 Marks)

Victory Polyfibres, a Partnership Firm, has earned a Gross Total Income of ₹ 300 Lakhs for the year ended 31.03.2014.There are no international transactions.

The above includes a profit of ₹ 220 Lakhs from an Industrial Undertaking having a turnover of ₹ 80 Crores. This is the fifth year and deduction under Section 80–IB of the Income Tax Act, 1961 is available to the extent of ₹ 200 Lakhs.

There are some grey areas in the taxation workings and hence the Assessee is contemplating to file the Return of Income on 07.12.2014, after seeking clarifications from Tax Experts.

Advise the Assessee–Company by working out the Total Income and Tax Payable, where the Return is filed on 31.10.2014 and when the same is filed on 07.12.2014.What is the practical solution as regards obtaining clarifications, which might or might not have an impact on the Total Income?

Solution: **Refer Para 11.1.2 in Page 11.2**

Assessee: Victory Polyfibres **Previous Year: 2013–2014** **Assessment Year: 2014–2015**

Status: Partnership Firm **Computation of Total Income & Tax Payable** **(₹ in Lakhs)**

Particulars	**Situation 1**	**Situation 2**
	Return Filed on **31.10.2014** [After the due date u/s 139(1)]	Return Filed on **07.12.2014** [After the due date u/s 139(1)]
Gross Total Income	300.00	300.00
Less: Deduction under Chapter VI–A – Deduction u/s 80–IB	Nil	Nil
Total Income	300.00	300.00
Tax on Total Income @30%	90.00	90.00
Add:		
Surcharge @ 10%	9.00	9.00
Education Cess @ 2%	1.98	1.98
SHEC @ 1%	0.99	0.99
Tax Payable	**101.97**	**101.97**

Consequences of not filing the Return on or before the due date:-

1. U/s 80AC, in order to claim deduction u/s 80–IB, it is mandatory to furnish Return of Income on or before due date for claiming deduction. Hence in both the Situations, as the Return is filed belatedly, the benefit of deduction u/s 80–IB is not available to the Assessee.
2. In case of return filed belatedly u/s 139(4), Assessee cannot file a Revised Return u/s 139(5).
3. Penalty u/s 272A(2) shall be levied at the rate of ₹ 100 for every day during which such fault continues.
4. Interest u/s 234A shall be charged at 1% per month or part thereof on tax payable on self–assessment.
5. Benefit of carry forward of losses u/s 72/73/74/74A is lost.
6. Failure to furnish Return of Income u/s 139(1), is liable to be proceeded u/s 276CC, if there is wilful delay.

Practical Solution:-

1. In order to avail the deduction u/s 80–IB, it is advised to file the Return within the due date u/s 139(1). In case of the corrections to be made in the computation of Income, the same can be done by the Assessee by way of filing Revised Return u/s 139(5).
2. If the return is filed within the due date u/s 139(1), i.e on or before 30th September 2014, the Total Income will be ₹ 100 Lakhs (by availing 80–IB deduction), and the Tax liability will be ₹ 30.90 Lakhs (i.e. No Surcharge in such case).

Alternative Assumption:
Though 30th September is the due date u/s 139(1) for filing the Return of Income, it can be assumed that for the AY 2014–15, the due date is on 31.10.2014 (say considering 1 month extension time to file the Return of Income) and solution can be worked out accordingly.

Question 1(b): Wealth Tax – Definition of Asset (10 Marks)

Examine with brief reason whether following are to be regarded as Assets while calculating the Net Wealth as on 31.03.2014:

(i) House given to a part–time employee of a Company who has substantial interest in the Company and whose Gross Salary is ₹ 50 Lakhs per annum.

(ii) Commercial Property let out for 300 days.

(iii) Jeep of the Company given to the Director for official use.

(iv) Land held as Stock–in–Trade. (Acquired on 30.04.2005)

(v) Urban Land lying vacant with incomplete Building.

(vi) Yachts owned by a Political Party.

(vii) Bullions held by the Reserve Bank of India.

(viii) Gold Deposit Bonds held by the Company, not being a Company registered u/s 25 of the Companies Act, 1956.

(ix) ₹ 49,999 Unrecorded Cash held by a Company.

(x) Helicopter owned by the Assessee and used exclusively for business purposes.

[Mere conclusion, without any brief reasoning, will not receive any credit.]. Status may be taken as Individual, unless indicated otherwise in the sub–division.

Solution: **Refer Para 29.1.5 in Page 29.5**

Valuation Date: 31.03.2014 **Assessment Year: 2014–2015**

Computation of Taxable Wealth

Nature of Asset	Asset?	Reasons
House given to a Part–time	Yes	Residential House allotted by a Company to its Employee / Officer / Executive, who is in **whole time employment**, and their Gross Salary is less than ₹ 10 Lakhs p.a. is exempted. In the given case, House is given to a Part–time employee hence not covered under the exemption.
Commercial Property Let Out for 300 days.	Yes	Residential House let–out for a period of 300 days or more during the previous year is excluded. **Only Residential House covered in the exclusion.**
Jeep given to the Director for official use.	Yes	**Motor Cars** cover all Motor Vehicles other than Heavy Vehicles. Hence, Buses, Trucks, Tempos are not considered as Motor Cars. However, Jeep, Sport Utility Vehicle (SUV), Multi Utility Vehicle (MUV), are classifiable as Motor Car. **[Southern Roadways Ltd 122 Taxman 126 (Mad.)**
Land held as stock in trade. (Acquired on 30/04/2005).	No	Any Urban Land held by the Assessee as Stock-in-trade, for a period of 10 years from date of acquisition. [it is assumed that it is Urban land].
Urban Land lying vacant with Incomplete Building.	No	Building for the purpose of Wealth Tax Act means Building which has been fully constructed and ready for occupancy or let out. Hence, Building under construction is not an asset u/s 2(ea). Incomplete Building neither falls within the meaning of building nor with the purview of urban land u/s 2(ea). Consequently, the Incomplete Building is not an asset chargeable to Wealth Tax. **[CIT vs Smt. Neena Jain 330 ITR 157 (P&H)]**
Yachts owned by a Political Party.	No	Yachts are asset u/s 2(ea). But, u/s 45, The Wealth Tax Act, 1957 does **not apply** to any Political Party as referred in Sec.13A of the Income Tax Act.

Nature of Asset	Asset?	Reasons
Bullions held by the Reserve Bank of India.	No	Bullions are assets u/s 2(ea). However, u/s 45, The Wealth Tax Act, 1957 does not apply to RBI incorporated under the RBI Act, 1934.
God Deposit Bonds held by the company, not being a Company registered u/s 25 of the Companies Act, 1956.	No	U/s 45, The Wealth Tax Act, 1957 does not apply to a Company registered u/s 25 of the Companies Act, 1956. However, Asset excludes Gold Deposit Bonds under Gold Deposit Scheme,1999.
₹49,999 of unrecorded cash held by a Company.	Yes	U/s 2(ea), Asset includes any amount not recorded in books of accounts, in case of all Assessees other than Individual and HUF.
Helicopter owned by the assessee and used exclusively for Business Purposes.	No	Aircraft includes Helicopter. However, u/s 2(ea), assets used by the Assessee for commercial purposes are excluded.

Question 2: Total Income – Chapter IV–D Deductions (16 Marks)

XYZ Ltd is engaged in the business of manufacturing fertilizers. Its Profit and Loss A/c shows a Net Profit of ₹ 500 Lakhs for the year ended 31.03.2014 after debiting and crediting the following items:

- **Depreciation provided in accounts as per Straight Line Basis is ₹ 30 Lakhs.**
- **Normal Depreciation allowable is ₹ 28 Lakhs. The Company has made addition to Machinery during the year to the extent of ₹ 100 Lakhs, in June 2013.**
- **The Company has made cash payments for purchases and expenditure as below:**
  On 04.06.2013 ₹ 5 Lakhs (Due to strike by Bank Staff)
  On 05.06.2013 ₹ 7 Lakhs (Due to cash demanded by the Supplier)
  On 30.09.2013 ₹ 10 lakhs (Half yearly closing for Bank, a Bank Holiday)
  Payment made to Transport Operator for hiring of lorry as follows:
  07.05.2013 = ₹ 50,000, 08.01.2014 = ₹ 75,000, 02.03.2014 = ₹ 32,000.
- **₹ 5 Lakhs contribution to a University approved and notified u/s 35(1)(ii).**
- **Sales Tax of ₹ 1.45 Lakhs, pertaining to the year ended 31.03.2013 was paid on 10.12.2013.**
- **Rent paid and Professional Charges to a consultant including Service Tax was ₹ 5,61,800 and ₹ 2,24,720 respectively. TDS was not deducted on the Service Tax portion for both the payments.**
- **The Company has imported 1,000 Kgs Raw Materials from a Supplier in US at the rate $75/Kg on 29.03.2013. The Exchange Rate was ₹ 59/$ when the Imports were made. The payment to the Supplier was made on 20.01.2014 when the exchange rate was ₹ 62/$. The Company had not entered into a Forward Contract to hedge the risk.**
- **The Company has also purchased goods of ₹ 55 Lakhs from M/s ABC Ltd, in which Directors have substantial interest. The Market Value of the goods is ₹ 54 Lakhs.**
- **The Company has incurred legal expenses for the following:**
  Issue of Bonus Shares ₹ 10 Lakhs.
  Alteration of Memorandum of Association ₹ 2 Lakhs (in connection with increase of Authorised Capital)
- **Donation paid to a Political Party is ₹ 25 Lakhs.**

Compute the Total Income and Tax Payable by the Company for the Assessment Year 2014–15. Ignore MAT Provisions.

Solution:

Assessee: ABC Ltd. **Previous Year: 2013–2014** **Assessment Year: 2014–2015**

Computation of Total Income **(Amount in ₹)**

Particulars		Deduction from Profit	Net Profit + Addition to Profit
Net profit as per Profit and Loss Account	**(Given)**		500,00,000
Adjustments for –			
Depreciation as per Accounts Straight Line Method Basis			30,00,000
Income Tax Depreciation allowable u/s 32		28,00,000	
Deduction u/s 35AD for Machinery acquired during June 2013	**(W.N.1)**	1,35,00,000	

	Particulars		Deduction from Profit	Net Profit + Addition to Profit
	Cash Payment on 04.06.2013–Bank Strike (Covered under Rule 6DD)	**(W.N.2)**	–	–
	Cash Payment on 05.06.2013 (Disallowed u/s 40A(3)	**(W.N.2)**		7,00,000
	Cash Payment on 30.09.2013–Bank Holiday (Covered under Rule 6DD)	**(W.N.2)**	–	–
	Payment to Transport Operator disallowable u/s 40A(3)	**(W.N.3)**		1,25,000
	Contribution to University approved and notified u/s 35(1)(ii)	**(W.N.4)**	3,75,000	
	Sales Tax Payment made on 10.12.2013 for the F.Y ended 31.03.2013	**(W.N.5)**	–	–
	Rent & Professional Charges Paid without deducting TDS on Service Tax Portion	**(W.N.6)**	–	–
	Foreign Exchange Loss [1000 kgs × (₹ 62 – ₹59) = ₹ 3,000	**(W.N.7)**	–	–
	Purchase from ABC Ltd. – Disallowable u/s 40A(2)	**(W.N.8)**		1,00,000
	Legal Expensed in respect of Issue of Bonus Shares	**(W.N.9)**	–	–
	Legal Expensed in respect of alteration of MOA	**(W.N.10)**		2,00,000
	Donation to political party	**(W.N.11)**		25,00,000
	Sub–Total		**1,66,75,000**	**5,66,25,000**
	Profits & Gains of Business or Profession			**3,99,50,000**
	Gross Total Income			
Less:	Deduction under Chapter VI A : Section 80GGB	**(W.N.11)**		(25,00,000)
	Total Income			**3,74,50,000**
	Tax Payable @ 30% on 3,74,50,000			**1,12,35,000**
Add:	**Surcharge @ 5% on 1,12,35,000**			**5,61,750**
Add:	**Education Cess @ 2% on 1,17,96,750**			**2,35,935**
Add:	**Secondary & Higher Education Cess @ 1%**			**1,17,968**
	Total Tax Payable			**1,21,50,653**
	Total Tax Payable (Rounded Off)			**1,21,50,650**

Working Notes:

1. U/s 35 AD, Weighted Deduction of 150% of the expenditure incurred will be allowed as deduction. Deduction Allowable = ₹ 100 Lakhs × 150% = ₹ 150 Lakhs. Depreciation already allowed @ 15% =₹15 Lakhs [₹ 100 Lakhs × 15%]. Balance Deduction allowable = ₹ 135 Lakhs [₹ 150 Lakhs – ₹ 15 Lakhs]

2. U/s 40A(3), Expenditure in respect of which aggregate payment made to a person in a day in excess of ₹20,000 made otherwise than by way of account payee cheque / Demand Draft is not allowable as deduction. But as per Rule 6DD, there are exceptions, and when payment is made on a day on which Banks were closed due to holiday or strike, the expenditure in Cash is allowed.

3. Limit u/s 40A(3) in case of Payment made for plying, hiring or leasing goods carriages is ₹ 35,000. Consequently payments made in excess of the above of ₹ 50,000 on 07.05.2013 & ₹ 75,000 on 08.01.2014 shall be disallowed.

4. U/s 35(1)(ii), weighted deduction of 175% is eligible for contribution made to any approved University. Total Deduction allowable = [₹ 5,00,000 × 175%] = ₹ 8,75,000. Deduction already debited in the books = ₹ 5,00,000. Further Eligible deduction = ₹ 3,75,000. [₹ 8,75,000 – ₹ 5,00,000].

5. Since Sales Tax has not been paid within the stipulated time u/s 43B during the Previous Year 2012-13, such payment would have not been allowed in its assessment for that Previous Year. Therefore, deduction will be available in the year of Payment. Since it is already debited to P&L A/c, no further adjustment is required.

6. Vide Circular 1/2014 dated 13th January 2014 issued by CBDT, Tax shall be deducted u/s Chapter XVII–B of the Act on the amount paid/ payable without including Service Tax Component. Consequently TDS need not be deducted on Service Tax portion. Hence no adjustment is required for non–deduction of TDS on Service Tax Portion.

7. Foreign Exchange loss on account of currency translation in is not a mere book entry, and is allowable as a deduction. Since it is already debited to P&L A/c, no further adjustment is required.

8. Provisions of Sec. 40A(2) shall be attracted in case of Payment made to any concern in which Directors are having Substantial Interest. Any **excessive** or **unreasonable sum** shall be disallowed.

9. Expenditure incurred in connection with the issuance of Bonus Shares is an allowable expenditure. **[General Insurance Corporation 205 CTR 280 (SC)].** Therefore, Legal Fees in relation to Issue of Bonus Shares is allowed.

10. Fees paid to the Registrar of Companies for enhancement of capital is a capital expenditure, not deductible u/s 37(1). **[Punjab State Industrial Development Corporation Ltd 225 ITR 792 (SC)].** Therefore, Legal Expenses in relation to alteration of Memorandum in connection with increase of Authorized Capital is not allowable.
11. Contribution to a Political Party is not allowable as deduction under Chapter IV–D, but allowable u/s 80GGB, and hence deductible from Gross Total Income.

Question 3(a): ALP in case of NJA transaction (8 Marks)

VKS International Ltd, the Assessee, has sold goods on 12.01.2014 to L Ltd. located in a Notified Jurisdictional Area (NJA), for ₹ 10.5 Crores. The sale price of identical goods sold to an unfamiliar customer in New York during the year was ₹ 11.5 Crores. While the second sale was on CIF basis, the sale to L Ltd was on F.O.B. basis. Ocean Freight and Insurance amount to ₹ 20 Lakhs.

India has a Double Taxation Avoidance Agreement with the USA. The Assessee has a policy of providing After–Sales Support Services to the tune of ₹ 14 Lakhs to all customers except L Ltd. The ALP worked out as per Cost Plus Method for identical goods is ₹ 12.10 Crores.

You are required to compute the ALP for the Sales made to L Ltd, and the amount of consequent increase, if any, in profits of the Assessee–Company.

Solution: **Similar to Illustration in Page 27.15**

1. Computation of Arm's Length Price of Products sold to L Ltd by VKS International Ltd.

	Particulars	₹ Crores	₹ Crores
	Price in a Comparable Uncontrolled Transaction		11.5
Less:	Adjustment for Differences –		
	(a) Freight and Insurance Charges	(0.20)	
	(b) After–Sales Support services	(0.14)	(0.34)
	Arm's Length Price Sales to L Ltd		**11.16**

2. Computation of Increase in Total Income of VKS International Ltd.

	Particulars	₹ Crores
	Arm's Length Price as above	11.16
Less:	Price at which actually sold to L Ltd.	10.50
	Therefore, **increase in Total Income of VKS International Ltd.**	**₹ 0.66**

Note:

1. ALP given under Cost Plus Model is not considered because ALP determined under Comparable Uncontrolled Transaction Method is considered as Most Appropriate Method in the given case.
2. U/s 92C, when more than one price is determined by the most appropriate method, the Arm's Length Price shall be taken to be the Arithmetical Mean of such prices. Since only one price is available in Most Appropriate Method, the same is considered here.
3. Second Proviso to Sec.92C(2) in relation to permissible variation of 3% is not applicable to transactions with person located in Notified Jurisdictional Area. As the Assessees's customer is in Notified Jurisdictional Area, the principle relating to permissible variation is not applicable.

Question 3(b): Case Study on Sec. 44AB (2 + 6 = 8 Marks)

Vishwa Textiles Ltd has convened a meeting of top Management in which the Taxation Manager and Finance Manager are also present. As Tax Auditor, you have also been convened to the meeting for the session relating to Tax Audit u/s 44AB of the Income Tax Act, 1961.
The Company plans to start a subsidiary for doing Chit Fund Business.

The Managing Director asked the Taxation Manager, "How are Gross Receipts / Turnover calculated for the purposes of Section 44AB, relating to Chit Fund Business?" The Taxation Manager replied that it was based on the Total Chit Collections during the year in question.

The Sales Manager pointed out in the meeting that Sales Return relating to a Sale effected in March, 2013 had been debited to the Sales Account in the current year. He wanted to know how this should be dealt with, in the particulars to be furnished in Form No. 3CD of the current year, i.e. Assessment Year 2014–15.

The Finance Manager had a different view relating to an item in Tax Audit Report of the Assessment Year 2013–14 and wanted some changes in Form No. 3CA of that year.

The Company has received a Subsidy of ₹ 10 lakhs from the State Government during the year for a Machinery purchased in 2010–11. The WDV of the Block as on 01.04.2013 was ₹ 12 Lakhs. The Chairman asked the forum "How will this Subsidy be reported in Form No. 3CD?

As Tax Auditor of the Company, you are required to –

(i) Identify the various issues raised relating to Section 44AB and requirements of particulars for Form No. 3CD, and

(ii) Suggest your views relating to the said issues.

Solution: **Refer Para 6.1.8 in Page 6.11**

Issue Raised	Principle	Requirement of Form No. 3CD
Determination of Turnover for Chit Fund Business	Aggregate of Commission, Brokerage, Service and other incidental Charges received in the business of Chit Funds.	Section 44AB is applicable if Total Sales or Turnover or Gross Receipts exceeds ₹ 1 Crore.
Treatment of Sales Returns of Prior Period	Sales Returns in normal course of business shall be deducted from the Sales Turnover.	**Clause 22(b)** – Particulars of Income / Expenditure of prior period credited / debited to P&L A/c is to be furnished. **Clause 28 (a)** – In case of Trading concern, Quantitative details of goods traded needs to be furnished. **Clause 28 (b) –** In case of Manufacturing concern, Quantitative details of Principal items of RM, FG and By–Products needs to be furnished.
Changes in Form 3CA for Prior A.Y	Since 3CA is an Audit Report, Changes in Form 3CA shall not be made by the Assessee.	NA
Subsidy from State Government	Subsidy received from State Government for a Machinery purchased during 2010–11, is of Capital Nature, and shall be reduced from the cost of Asset.	The amount of Subsidy or grant or reimbursement, by whatever name called received during the year, shall be deducted from WDV and to be shown in Clause 14 (d)(iii).

ANSWER ANY FOUR FROM THE FOLLOWING FIVE SUB–DIVISIONS in Q.No.4

Question 4(a): Allowability of Referral Fee Paid to Doctors (4 Marks)

X & Co. Diagnostic Centre P Ltd. has claimed Referral Fee paid to doctors as Revenue Expenditure for the Assessment Year 2014–15. However, TDS has been deducted u/s 194H of the Income Tax Act, 1961 for the said payments. The Assessing Officer proposes to disallow such expenditure. Examine the correctness of the action of the Assessing Officer.

Solution: **Refer *Kap Scan & Diagnostic Centre* Case Law in Page 6.65**

1. **Principle**: Commission paid to Doctors by a Diagnostic Center for referring patients for Diagnosis cannot be allowed as Business Expenditure. Since such activity is contrary to the provisions of Indian Medical Council Regulations.**[Kap Scan and Diagnostic Centre P Ltd (2012) 344 ITR 476]**

2. **Conclusion:** Based on the above, the action of the Assessing Officer in disallowing the Referral Fee paid to Doctors is valid. Whether TDS is deducted or not, is not relevant in this regard.

Question 4(b): TDS Provisions – Section 194–A & 195 (2 × 2 = 4 Marks)

Discuss whether tax has to be deducted at source under the provisions of the Income Tax Act, 1961 in the following situations, which have taken place during the year ended 31.03.2014:

(i) M/s Jiva & Co. a Partnership Firm, pays a sum of ₹ 43,000 as Interest on Loan borrowed from Indian Branch of a Foreign Bank.

(ii) Above Firm has paid ₹ 14,000 as Interest on Capital to Partner Mr. A, a Resident in India and ₹ 22,000 as Interest on Capital to Partner Mr. B, a Non–Resident.

Solution: **Refer Sec. 194A in Page 41.9& Sec. 195 in Page 41.29**

1. **Principle:**
   (a) Under Sec.195, TDS needs to be deducted on payment of **Interest** (excluding Interest u/s 194LB / 194LC / 194LD), including Interest on Securities, or any **other sum chargeable to Income–Tax in India**, **not being Salaries.**
   (b) U/s 194A, TDS is not required on Interest credited or paid to a **Partner** (who is resident), by the **Firm**.

2. **Conclusion**: In the above case, TDS needs to be deducted u/s 195 on Payment made to a Indian Branch of a Foreign Bank, and on Interest Paid to Mr. B being non–Resident.

Question 4(c): Exemption u/s 54F on Sale of Depreciable Assets (4 Marks)

Mrs. Priya, a Resident Individual, sold on 03.06.2013, Depreciable Assets held for more than 36 months and invested the proceeds on 30.09.2013 in a Residential House Property to claim exemption from Capital Gains.

Examine the validity of the Order of the Assessing Officer in denying her the exemption u/s 54F of the Income Tax Act, 1961. Mrs. Priya does not own any other Residential House.

Solution: **Refer Rajiv Shukla Case Law in Page 7.40**

1. **Provision:** Depreciable Assets held for more than 36 months shall be considered as Long Term Capital Assets and on such sale, it shall be considered as Short Term Capital Gains based on the provisions of Sec.50. Section 50 is applicable only for the purposes of Section 48 and 49 and not for any other section. Sec.54F being an independent section will not be bound by the provisions of Sec.50. So, exemption u/s 54F is available for Depreciable Assets sold after 36 Months. **[CIT vs Rajiv Shukla 334 ITR 138 (Del.)]**

2. **Conclusion**: Since Mrs. Priya held the depreciable assets for more than 36 months, and she does not own any other residential House Property on the date of transfer, benefit of Sec.54F is available. The order of the Assessing Officer is not valid.

Question 4(d): Order of Settlement Commission (4 Marks)

X & Co Ltd. had made an application to the Settlement Commission. The issue in the said application related to Cash Credits in the Books of Account. The Commission passed an Order making addition to the Income on the basis of difference in Gross Profit Rate adopted, which was neither an issue in the application nor in the Report of the Commissioner of Income Tax. Discuss the validity of the Order of the Settlement Commission.

Solution: **Refer Para 2(b) in Page 37.7**

1. **Order:** The Settlement Commission may, in accordance with the provisions of this Act, pass such order as it thinks fit.

2. **Scope of Order:** Matters covered by the application, and **any other matter** relating to the case not covered by the application, **but referred to in Commissioner's report**.

3. **Conclusion:** In the above case, the Issue covered in the Order of Settlement Commission is neither covered in the Application nor in the Report of the Commissioner. Hence, the order passed by the Settlement Commission is **not valid.**

Question 4(e): TDS u/s 192 **(4 Marks)**

A Foreign Company seconded some employees to the Assessee, an Indian Collaborator. The Assessee had not deducted Tax at source on the Home Salary / Special Allowance/s (Education Allowance or Retention Allowance) payments made by Foreign Company / HO to its employees (expatriated to India) outside India in Foreign Currency. The Revenue Authorities, holding the Assessee as an 'Assessee–in–default' u/s 201 of the Income Tax Act, 1961, levied Interest and Penalty on it. Is the same justified?

Solution: **Refer *CIT vs Eli Lilly & Co* Case Law Page 41.5**

1. **Provision: TDS** is to be **deducted** u/s 192 on **Retention Salary** provided by **Foreign Company** to its employees **who work in India** for the Joint Venture in which such Foreign Company is also a partner, as the Retention Salary is deemed to accrue or arise in India u/s 9(1). **[CIT vs Eli Lilly and Company (India) Pvt Ltd (2009) 312 ITR 225]**
2. **Conclusion:** In the given case, as the Salary Income to the seconded employees are deemed to Accrue or arise in India, Indian Collaborator is liable to deduct TDS. Since TDS is not deducted by the Assessee, Revenue is justified in treating the Assessee as an 'Assessee–in–default'.

Question 5(a): Re–opening Assessment vs Other Options **(4 + 4 = 8 Marks)**

The Regular Assessment of MNO Ltd for the Assessment Year 2012–13 was completed u/s 143(3) on 13th April 2013. There was an Audit Objection by the Revenue Audit Team, that interest on loan should be partly disallowed as there was diversion on borrowed fund to Sister Concern without charge of Interest.

Based on the above facts:

(i) State, with reasons, whether the Assessing Officer can issue Notice u/s 148 (on 12th March 2014) on the basis of Audit Objection of the Revenue Audit team.

(ii) If the action stated in (i) above is not permitted, what is the option open to the Revenue Department to deal with the said Audit Objection?

Solution: **Same as Illustration in Page 34.10**

1. **Re–opening of Assessment:**
   (a) An assessment cannot be re–opened u/s 147 on the basis of a change of opinion, if no extra facts have come to light. **[Garden Silk Mills (P) Ltd 237 ITR 668 (Guj.)]**
   (b) The AO should have the reason to believe that income chargeable to tax has escaped assessment. The belief should be that of the AO and **not** the Audit Party.
   (c) The opinion of the audit party on a particular statutory provision is not valid information for initiating re–assessment proceedings. **[Juhi Metal Works 263 ITR 287 (All.)]**
   (d) **Conclusion:** In view of above, audit objection raised cannot be the basis for re–opening assessment.
2. **Options open to Revenue:**
   (a) Given issue deals the allowability of Interest Expenditure on borrowed funds which is in turn given to sister concern without charge of Interest. In **S.A. Builders Ltd Vs CIT 206 CTR 631**, The Supreme Court pronounced that there should be **nexus** between the expenditure and the purpose of the business, which need not necessarily be the business of the Assessee himself.
   (b) Also, the power of the CIT is wide enough to make or cause to be made any enquiry as considered necessary to find out that the assessment order is not erroneous nor it is prejudicial to the interests of revenue. In view of the above, the Department can use the option / rights of the CIT u/s 263.

Question 5(b): Remedies to Assessee – Time Limits **(2 × 4 = 8 Marks)**

An Assessee, who is aggrieved by all or any of the following orders, is desirous to know the available remedial measures, and the Time Limit against each, under the Income Tax Act, 1961:

(i) Passed u/s 143(3) by Assessing Officer,

(ii) Passed u/s 263 by the Commissioner of Income Tax,

(iii) Passed u/s 272A by the Director General, and

(iv) Passed u/s 254 by the Income Tax Appellate Tribunal.

Advise him suitably

Solution: **Same as Illustration in Page 39.17**

Orders passed	Remedies Available	Time Limit
Order u/s 143(3) by the Assessing Officer	**In case of any error apparent on the record:** Application for rectification of mistake **u/s 154**, to the Assessing Officer himself.	Any time **within 4 years** from the end of the Financial Year in which order is passed.
	In case of failure to claim deduction or any other benefit: Application for Revision to the CIT **u/s 264**	Within **1 year** from the date of receipt of order.
	In any other case: Appeal to the CIT (A) **u/s 246A**	Within **30 days** from the date of receipt of order.
Revision u/s 263 made by the CIT	Appeal to the ITAT	Within **60 days** from the date of communication of order.
Order u/s 272A by Director General	Appeal to the ITAT	Within **60 days** from the date of communication of order.
Order u/s 254 by ITAT	**In case of any error apparent on the record:** Application for rectification of mistake u/s 254 (2)	Any time within **4 years** from the date of the order.
	In case of question of law: Appeal to the High Court of competent jurisdiction	Within **120 days** from the date of communication of the order.
	In case of question of fact: No remedy is available. The order passed by the ITAT is final.	NA

Question 6(a): Depreciation, Deduction u/s 32AC **(8 Marks)**

Compute the quantum of Depreciation available u/s 32 of the Income Tax Act, 1961 and any other benefit available in respect of the following items of Plant and Machinery purchased by PQR Textile Ltd. which is engaged in the manufacture of Textile Fabrics, during the year ended 31.03.2014:

Particulars	₹ Crores
New Machinery installed on 01.05.2013	84
New Windmill purchased and installed on 18.06.2013	22
Items purchased after 30th November, 2013:	
Lorries for transporting goods to Sales Depots	3
Fork–Lift–Trucks, used inside Factory	4
Computers installed in Office Premises	1
Computers installed in Factory	2
New Imported Machinery	12

The new imported Machinery arrived at Chennai Port on 30.03.2014 and was installed on 03.04.2014. All other items were installed during the year ended 31.03.2014. The Company was newly started during the year.

Also compute the WDV of the various Block of Assets. Will your answer be different if the above Assessee were a Partnership Firm?

Solution:

Assessee: PQR Textile Ltd. **Previous Year: 2013–2014** **Assessment Year: 2014–2015**

Depreciation as per Income Tax Act, 1961 **₹ in Lakhs**

Nature of Block	New Machinery	Windmill	Lorries	Fork–lift–Trucks	Computers in Office	Computers in Factory
Rate of Depreciation	**15%**	**15%**	**15%**	**15%**	**60%**	**60%**
Additions Made during the Year						
Put to use < 180 days			300.00	400.00	100.00	200.00
Put to use > 180 days	8,400.00	2,200.00				
Deletions	–	–	–	–	–	–
Net Block Value	**8,400.00**	**2,200.00**	**300.00**	**400.00**	**100.00**	**200.00**

Nature of Block	New Machinery	Windmill	Lorries	Fork–lift–Trucks	Computers in Office	Computers in Factory
Normal Depreciation						
a. Asset Put to use < 180 days (50%)			22.50	30.00	30.00	60.00
b. Put to use > 180 days	1260.00	330.00				
Additional Depreciation @ 20%						
a. Asset Put to use < 180 days (50%)				40.00	**W.N.1**	20.00
b. Put to use > 180 days	1680.00	440.00	**W.N.1**			
WDV as on 31.03.2014	**5460.00**	**1430.00**	**277.50**	**330.00**	**70.00**	**120.00**

2. Computation of Deduction u/s 32AC **(₹ in Lakhs)**

Particulars		
For Assessment Year 2014–15		
Total Investment in Eligible Assets PY 2013–14 [₹ 8400+₹ 2200+₹ 200]		10,800.00
Deductions for PY 2013–14 [₹ 10,800.00 Lakhs × 15%]		**1,620.00**
For Assessment Year 2015–16		
Total Investment from 01.04.2013 to 31.03.2015 [₹ 10,800.00 Lakhs + ₹ 1200.00 Lakhs]		12,000.00
Deduction @ 15% of above	1800.00	
Less: Deduction Claimed in PY 2013–14	(1620.00)	**180.00**

Notes:

1. Road Transport Vehicle and Office Appliances (Computers used in Office) are **not** eligible to claim Additional Depreciation.
2. Enhanced Depreciation of 80% to Windmills shall be available only upto 31.03.2012.
3. U/s 32AC, 15% of Cost of New Asset acquired and installed between 01.04.2013 to 31.03.2015, if Aggregate Amount of Actual Cost of such New Assets exceeds ₹100 Crores, is allowable as a Deduction to a company engaged in the business of manufacture or production of any article or thing, acquired and installs New Asset. However, New Asset does not include any Office Appliances including Computers or Computer Software or Any Vehicle.
4. Fork–lift–Trucks, being in the nature of Vehicles, are **not** eligible for benefit u/s 32AC.
5. The new imported machinery was only installed after 31.03.2014. Hence, the benefit of Sec. 32AC can be claimed only during A.Y 2015–16.

Treatment if Assessee is a Partnership Firm: Deduction u/s 32AC will not be allowable, since Sec.32AC applies only to a **Company** engaged in the business of manufacture or production of any article or thing.

Question 6(b): Business Income – Taxability of Items **(8 Marks)**

Examine the taxability or allowability or otherwise in the following cases while computing Income under the Head "Profits and Gains from Business or Profession" to be declared in the Return of Income for the Assessment Year 2014–15:

(i) Amount received towards Power Subsidy with a stipulation that the same is to be adjusted in the Electricity Bills.

(ii) Donations received by a person in the course of carrying on vocation, from his followers.

(iii) Profit derived by an Assessee engaged in carrying the business as dealers in Shares, on exchange of the Shares held as Stock–in–Trade of one Company with the Shares of other Company.

(iv) The amount of Margin Money forfeited by a Bank on the failure of its Constituents of not taking the delivery of the Shares purchased by such Bank on their behalf.

Solution: **Same as Illustration in Page 6.5**

	Taxability/ Allowability
(i)	Power Subsidy received by an Assessee is revenue in nature, since it goes to reduce the Electricity Bills and hence **taxable u/s 28. [Rajaram Maize Products 251 ITR 427 (SC)]**
(ii)	The Assessee carried on a vocation of practicing against atheism and was engaged in a movement for the spread of religion. Sum received as donations from his friends, shall be treated as Business or Professional Income. **[Dr. K. George Thomas 156 ITR 412]**
(iii)	Profit derived from sale and purchase of securities by a Dealer in Shares will be treated as **Business Income,** and chargeable to tax under the head Profits and Gains of Business or Profession.
(iv)	Forfeiture of Margin Money deposits represents Bank's Business Income. [**Lakshmi Vilas Bank Ltd 220 ITR 305 (SC).]** It cannot be reduced from the cost of the investment for which such margin money was received.

Question 7(a): Relief u/s 91 **(8 Marks)**

The following are the particulars of Income earned by Miss Vivitha, a Resident Indian aged 25, for the Assessment Year 2014–15:

Particulars	₹ Lakhs
Income from playing Snooker in Country L	**12.00**
Tax paid in Country L	**1.80**
Income from playing Snooker Tournaments in India	**19.20**
Life Insurance Premium paid	**1.20**
Medical Insurance Premium paid for her father aged 62 years (paid through credit card)	**0.25**

Compute her Total Income and tax payable by her for the Assessment Year 2014–15. There is no Double Taxation Avoidance Agreement between India and Country L.

Solution: **Similar to Illustration in Page 28.6**

Assessee: Miss. Vivitha **Previous Year: 2013–2014** **Assessment Year: 2014–2015**

Status: Resident Indian **Computation of Total Income and Tax Payable**

	Particulars	₹	₹
	Profits and Gains from Business or Profession		
	(a) Income from playing outside India (Country L)	12,00,000	
	(b) Income from India	19,20,000	
	Taxable Profit or Gains from Business or Profession		31,20,000
	Gross Total Income		**31,20,000**
Less:	**Chapter VI A Deduction**		
	U/s 80C – Contribution to PPF (allowed upto a maximum of 1,00,000)	(1,00,000)	
	U/s 80D – Mediclaim for Father – Senior Citizen (paid other than by way of Cash)	(20,000)	(1,20,000)
	Total Income		**30,00,000**
	Tax on Total Income (1,30,000 + (30,00,000 – 10,00,000) × 30%)		7,30,000
Add:	Education Cess @ 2%		14,600
Add:	Secondary and Higher Education Cess @ 1%		7,300
	Total Tax Payable		**7,51,900**
	Average Rate of Indian Tax $\frac{7,51,900}{30,00,000}$	25.063%	
	Average Rate of Foreign Tax $\frac{1,80,000}{12,00,000}$	15.000%	
Less:	**Relief u/s 91** @ 15% of Foreign Income of ₹ 12,00,000 (Least of the above)		1,80,000
	Net Tax Payable (Rounded Off u/s 288B)		**5,71,900**

Question 7(b): TDS on Landing & Parking Charges (4 Marks)

"Come Air Ltd" has paid a sum of ₹ 12 Lakhs during the year ended 31.03.2014 to Airport Authority of India towards Landing and Parking Charges. Is the Company required to deduct any Tax at source from such payment? Is so, what is the Rate of TDS?

Solution: **Same as Illustration in Page 41.20**

This issue is governed by two views given below –

1. Payments made for Landing and Parking Charges would be deemed to be Rent, and liable for TDS u/s 194–I. **[CIT Vs Asiana Airlines (2009) 175 Taxman 177 (Del.)].** If it is Liable for TDS u/s 194–I, TDS needs to be deducted at the rate of 10%. Consequently ₹ 1,20,000 shall be deducted as TDS.
2. **Alternative View:** Landing and Parking Charges paid to Airport Authority is **not** Rent within the meaning of Section 194–I. **[Singapore Airlines Ltd (2012) 24 Taxmann 200 (Mad)]**

Question 7(c): Cross Transfer–Clubbing (4 Marks)

Mr. Vasudevan gifted a sum of ₹ 6 Lakhs to his brother's wife on 14.06.2013. On 12.07.2013, his brother gifted a sum of ₹ 5 Lakhs to Mr. Vasudevan's wife. The gifted amounts were invested as Fixed Deposits in Banks by Mrs. Vasudevan and wife of Mr. Vasudevan's brother on 01.08.2013 at 9% Interest.

Discuss the consequences of the above under the provisions of the Income Tax Act, 1961 in the hands of Mr. Vasudevan and his brother.

Solution: **Refer Para 9.1.2 in Page 9.5**

1. **Principle**: U/s 64, Income from assets transferred in a cross–transfer would be assessed in the hands of the Transferor, if –
   (a) Transfers are so intimately connected to form part of a single transaction, and
   (b) Each transfer constitutes consideration for the other by being mutual or otherwise.
2. **Legal Position**: When two transactions are inter-connected and are parts of the same transaction in such a way that it can be said that the **circuitous method** was adopted as a device to evade tax, the implication of clubbing provisions would be attracted.**[CIT Vs Keshavji and Moraji 66 ITR 142 (SC)]**
3. **Inference:** In the given case, income accruing from Fixed Deposits should be included in the Total Income of Mr. Vasudevan and in the hands of his Brother, as the gifts are Indirect Transfers of their income yielding assets, to their Spouse respectively, and such transfer has been made so as to reduce their burden of taxation.